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C O N F I D E N T I A L SECTION 01 OF 03 MOSCOW 000541

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TAGS: [ETRD](#) [EAGR](#) [ECON](#) [WTO](#) [RS](#)
SUBJECT: RUSSIAN OFFICIAL EXPLAINS DUTY INCREASES FOR CARS
AND HARVESTERS

REF: A. MOSCOW 439
[B. MOSCOW 334](#)
[C. 08 MOSCOW 3745](#)
[D. MOSCOW 101](#)
[E. 08 MOSCOW 3678](#)

Classified By: ECON M/C Eric T. Schultz, Reasons 1.4(b,d).

SUMMARY

[1](#)1. (C) Alexander Rakhmanov, Director of the Department of Automotive and Agriculture Equipment Policy at the Ministry of Industry and Trade, acknowledged to us that the recent duty increases for cars and harvesters were meant to protect domestic producers from import competition and help them weather the global economic crisis. Rakhmanov stated that GOR financing programs for economy class cars would be open to foreign car makers with domestic production operations. However, the GOR would no longer subsidize financing for purchases of foreign-produced agricultural equipment. He noted that the GOR would consider additional protectionist measures in these sectors over the next several months as economic conditions warranted. END SUMMARY.

Car Duties: Domestic Producers Asked for It

[1](#)2. (C) Rakhmanov said the GOR raised duties on automobiles to improve competitive conditions for domestic car producers and stimulate greater domestic production. Before raising the duties, Rakhmanov said that the GOR had consulted with several domestic and foreign automakers with production operations in Russia. Many companies, including GM, had urged the GOR to impose greater restrictions on used, right-hand drive vehicle imports, claiming that they suppressed sales of locally produced new cars. He noted that there were nearly 600,000 used vehicles imported into Russia in 2008, a situation that the GOR could no longer "tolerate." Rakhmanov downplayed the impact of the "marginal" duty increases on new imported cars. He said the GOR also wanted to encourage further investment in domestic production from the major foreign car makers through the new import duties.

Financing Programs for Automobiles

[1](#)3. (C) Rakhmanov said that the February 10 announcement of

GOR subsidized lending for consumers wishing to purchase inexpensive, domestically produced cars (Ref B), was intended to help "budget" consumers afford a car. Rakhmanov noted that the GOR would subsidize up to two thirds of the "refinancing rate" on commercial loans under the program. (N.B. As discussed in Ref B, Russia's four major domestic vehicle manufacturers are in deep financial straits. Overall domestic demand for cars has declined rapidly in the wake of the global economic crisis. In January 2009, domestic production of cars fell by 80% compared to January 2008; car imports also declined, by 73%.)

14. (C) Rakhmanov said that the subsidized financing program would not discriminate against foreign firms that produced domestically. The purchase of any domestically produced car that cost less than 350,000 rubles would be eligible for the subsidy. In addition to the Russian manufacturers, Ford, VW and Fiat would stand to benefit most from the program. Rakhmanov acknowledged that the number of cars that could be financed under the program was finite. The GOR would provide no more than 2 billion rubles (\$55.6 million) in subsidized financing in 2009.

Additional Measures

15. (C) Rakhmanov said that the GOR was also planning to support the automobile sector through GOR purchases of domestically produced cars. The 12.5 billion rubles (\$347 million) procurement announced on February 10 (Ref B) would

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be limited solely to Russian domestic producers, but foreign firms that produce cars within Russia would still be able to participate in earlier GOR tenders that were announced during the 4th quarter of 2008. The GOR was also considering a second tranche of state procurements of trucks and buses later in 2009.

16. (C) Rakhmanov added that the GOR had no concrete plans for any further direct equity investments in Russia's car companies (besides the existing GOR stakes in Avtovaz and Kamaz), but that direct GOR ownership might be considered in the future if the company's economic prospects or financial conditions worsened. There were 750,000 people currently employed in the automobile industry, with an additional 2.5 million jobs in related businesses and upstream industries. The GOR would not allow the industry to collapse.

Harvester Duty Increase Was Necessary

17. (C) Rakhmanov admitted that the recent duty increase on harvesters breached the November 2006 U.S.-Russia market access agreement and side letters signed as part of Russia's WTO accession process. However, he argued that the conditions in the industry had materially changed since 2006. Russian companies now produced all classes of harvesters and the GOR believed that Russia, as a "key" agricultural country, should continue to produce harvesters. While the duty increase was admittedly an "unpleasant blow" to John Deere and other major U.S. and EU producers, the GOR was facing the grim prospect that domestic production of harvesters would drop precipitously in 2009 without some protection from import competition.

18. (C) Rakhmanov said he hoped the major foreign firms would ultimately choose to set up production of agricultural equipment within Russia, which would be a way around the new duties. In that regard, he noted that the GOR was finalizing a plan to offer beneficial investment terms to global agricultural equipment manufacturers willing to set up production and assembly operations in Russia.

Financing of Foreign Agriculture Equipment Gone

¶9. (C) Rakhmanov also confirmed that the GOR would no longer subsidize the financing of foreign agricultural equipment purchases, given the GOR's increasingly limited budgetary resources (Ref A). However, the GOR would continue to subsidize financing for domestic equipment purchases, and would cover all but one percent of the interest rate on commercial loans and leases for domestically produced equipment. In addition, Rakhmanov said recent GOR infusions of capital into Russia's major agricultural banks were subject to a condition that the funds only be used to purchase domestically produced agricultural equipment, rather than foreign equipment (i.e., a "Buy Russian" provision). Rakhmanov, added, that the GOR might consider partially lifting the financing moratorium for foreign agricultural equipment for which there was no domestically produced equivalent product.

Extending the Duties

¶10. (C) Noting that the increased duties on both cars and harvesters would be in effect for an initial temporary period of nine months, Rakhmanov said that the GOR would revisit the duties in September 2009 and determine, based on market conditions at that time, whether to maintain the duties or let them expire. In particular, for the harvesters duty, even if the GOR extended the duty beyond the nine month period, Rakhmanov noted that it would ultimately return to a lower level after Russia's accession to the WTO.

Comment

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¶11. (C) The duty increases on harvesters and cars are blatantly protectionist. The former violates not only the November 2006 U.S.-Russia bilateral agreement establishing a substantially lower duty rate, but also the consultation provisions of the EU-Russia Partnership and Cooperation Agreement. The new "Buy Russian" financing policies for automobiles and agricultural equipment are also problematic. They will clearly harm U.S. imports of agricultural equipment (Ref A). Russian officials are aware of the country's international trade commitments, but they are far more concerned with shielding vulnerable domestic producers from import competition and the global economic crisis, and avoiding mass layoffs at Russian production facilities.
BEYRLE